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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

OFFICE OF
THE CHAIRMAN

April 20, 1994

92-26

The Honorable Herb Klein
U. S. House of Representatives
1728 Longworth House Office Building
Washington, D.C. 20515-3008

Dear Congressman Klein:

Thank you for your recent letter regarding the Commission's cable rate regulations and the rate increases experienced by some of your constituents since the Commission's initial regulations went into effect.

In our initial rate regulation order, which became effective September 1, 1993, the Commission attempted to ensure that all cable operators would charge reasonable rates for regulated services and equipment. To achieve this goal, the Commission first ascertained the average rates charged by systems that face effective competition. The rate order required cable systems whose rates were above this benchmark level to reduce their rates by up to 10 percent. The Commission estimated that as a result of this order, two-thirds to three-quarters of cable subscribers would see an average 10 percent decrease in their bills for regulated services and equipment.

As further protection for consumers, the Commission implemented a cable rate freeze, which was recently extended until May 15, 1994. Under the freeze, the average monthly subscriber bill for cable services and associated equipment subject to rate regulation under the Cable Act of 1992 may not increase above the level determined under rates in effect on April 5, 1993. No change in rates is permitted that increases an operator's average subscriber revenues. However, operators may raise or lower individual rate components such as specific tier or equipment charges in order to come into compliance with the new rules. Nothing in the rules requires cable systems to raise their rates for any service or any piece of equipment rented to subscribers.

As the Commission intended, the implementation of regulation resulted in a substantial net reduction in the cable companies' average regulated revenue per subscriber. However, as they performed the calculations required by the rules, many operators discovered that while their rates for some services were above the reasonable level established by the Commission, rates for

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other services were below the maximum reasonable rate. In this situation, the terms of the rate freeze permit, but do not require, the cable operator to increase the rate for low-priced service, but not above the reasonable level, in order to offset the rate decrease that it must make for the high-priced services. As a result, some subscribers who do not take all of the regulated services and equipment offered by their cable operator have experienced rate increases.

On February 22, 1994, the Commission announced that it was adopting new rate regulations for regulated cable services which are expected to be effective in mid-May 1994. These new rate regulations are expected further to reduce the rates paid by most cable subscribers. The enclosed press releases explain more fully the newly adopted rate regulations.

Briefly, the new rate regulations will provide for a revised benchmark rate, which was calculated by applying a stronger statistical and economic model to the data on rates charged in competitive systems that was previously collected by the Commission. In general, prices for regulated services of all cable systems must be lowered 17 percent from September 30, 1992 rates. Cable operators whose rates are at or below the new benchmark and small cable operators will have a transition period during which they will not be required to lower their prices by the full 17 percent pending the completion of cost studies. In addition, if a cable operator believes that its costs of service are unusually high, the cable operator **may** request relief from application of the new benchmark rates by making a cost-of-service showing. In this instance, the cable operator's rates will be based on interim rules setting forth allowable costs and a reasonable return on the allowable ratebase.

You also expressed concern about FCC Form 329, which consumers are required to use in order to complain to the Commission about cable programming service rates. In January of this year, the Commission promulgated new, simplified Form 329 in order to correct problems that had turned up with use of the old form. A copy of the new Form 329 is enclosed for your information. Since introducing the new form, the proportion of forms that have been correctly completed by consumers has increased substantially, and the Commission has received very few complaints about the new form. Of course, we will gladly consider any further suggestions you may have for making the Commission's procedures more accessible to the public.

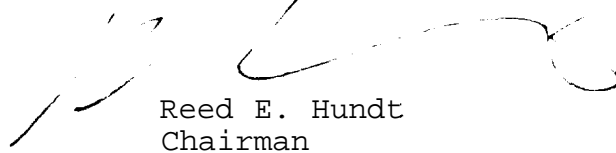
Once **again**, thank you for supporting the Commission's efforts to implement a regulatory regime that protects consumers

The Honorable Herb Klein

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from unfair pricing. The Commission's new rate regulations should achieve this goal, while providing incentive for cable operators to invest and innovate for the ultimate benefit of consumers.

Sincerely,

A handwritten signature in dark ink, appearing to read "Reed E. Hundt", with a long, sweeping horizontal stroke extending to the right.

Reed E. Hundt
Chairman

Enclosures



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EXECUTIVE SUMMARY

February 22, 1994

Implementation of Sections of the Cable Television Consumer
Protection and Competition Act of 1992;
Report and Order and Further Notice of Proposed Rulemaking
MM Docket No. 93-215

The Commission today announces its adoption of interim rules to govern cost of service proceedings initiated by cable operators. The Commission anticipates that most cable operators will set rates by applying the revised competitive differential approach announced today, rather than through the cost of service approach. It recognizes, however, that the cost of service approach may be appropriate for some operators. The interim cost of service rules are carefully designed to ensure that subscribers are charged reasonable rates, and that cable operators have both the opportunity for adequate recovery, and incentives to upgrade their systems and introduce new services and capabilities.

Cost of service proceedings may be elected by cable operators facing unusually high costs. Those operators will have their rates based on their allowable costs, in a proceeding based on principles similar to those that govern cost-based rate regulation of telephone companies. Under this methodology, cable operators may recover, through the rates they charge for regulated cable service, their normal operating expenses and a reasonable return on investment.

Requirements Governing Ratebase

Used and Useful, Prudent Investment S t - : To be included as part of "plant in service," the largest component of the ratebase, plant must be used and useful in the provision of regulated cable service, and must be the result of prudent investment. Under these standards, the plant must directly benefit the subscriber and may not include imprudent, fraudulent, or extravagant outlays.

Modified Original Cost Valuation: Plant in service will generally be valued at its cost at the time it was originally used to provide regulated cable service. In order to permit a

simplified method of cost valuation in the case of systems that were **acquired** by the current operator, plant may be valued at the book cost of tangible assets and allowable intangible assets at the time of acquisition.

Excess Acquisition Costs: Acquisition costs above book value are presumptively excluded from the ratebase. The Commission believes that, in most cases, excess acquisition costs such as "goodwill" represent the value of the monopoly rents the acquirer hoped to earn during the period when the cable system was effectively an unregulated monopoly. These monopoly rents would not be recoverable from customers where **effective competition exists**, the couchstone for rate regulation under the Cable Act. The Commission also recognizes that there may be situations where operators could make a cost-based **showing** to rebut a **presumption** of excluded acquisition costs. The Commission will consider such showings under certain circumstances.

Additions to Original and Book Costs: Some costs incurred after original costs and some intangible, **above-book costs** may be allowed. For example, cable operators may have incurred start-up losses in the early years of operating their systems. The Commission will permit reasonable start-up losses to be added to original costs recoverable by the operator, limited to losses actually incurred during a two-year start-up period and amortized over a period no longer than fifteen **years**. Certain other intangible acquisition costs above book value, **including** costs of obtaining franchise rights and **some start-up** organizational costs such as costs of customer lists, will **also** be allowed. Other intangible **acquisition costs** will be presumptively disallowed. Carriers may challenge this presumption, **however**, by showing a direct relationship between the costs incurred and benefits to customers.

Plant Under Construction: Valuation of **"plant under construction"** will use a traditional capitalization method. Under this approach, **plant** under construction is excluded from the ratebase. The **operator capitalizes an allowance** for funds used during **construction (AFUDC)** by **including it in the cost of construction**. When **plant** is placed into **service**, the regulated portion of the **cost of construction, including AFUDC**, is included in the **ratebase and recovered** through depreciation.

Cash Working Capital: The Commission expects to allow operators flexibility in **choosing** a method of determining the costs of funding day-to-day operations, as **embodied** in cash working capital. Because **cable operators** generally bill for regulated services in advance, the Commission will presume **zero** cash working capital. Operators may **use one of several methods** for overcoming this presumption, including the Simplified Method for telephone carriers in Section **65.820(e)** of the Commission's

Rules.

Other Costs - Excess Capacity, Cost Overruns, and Premature Abandonment: A cable operator may include in the **ratebase** excess capacity that will be used for regulated **cable service** within one year. Cost overruns are presumptively disallowed, but operators may overcome this presumption by showing that the costs were prudently incurred. Costs associated with premature abandonment of plant are recoverable as **operating expenses**, amortized over a term equal to the remainder of the original expected life.

Permitted **Expenses**

Operating Expenses. The Commission **adopts** standards that will permit operators to recover the ordinary **operating expenses** incurred in the provision of regulated cable services.

Depreciation. The Commission will not prescribe cable **system** depreciation rates, but will evaluate the reasonableness of depreciation rates submitted by cable operators.

Taxes. **Corporations** may include an allowance for income taxes at the statutory rates in their cost of service showings. Subchapter S corporations, partnerships, and sole proprietorships may also include an allowance for taxes based on earnings retained in the **regulated firm**.

Rate of Return

The Commission establishes an interim industry-wide rate of return of **11.25%** for presumptive use in cable cost of service proceedings. It solicits comment on whether this interim rate should be made permanent.

Rate **Development and Cost Support**

Accounting Requirements: The Commission adopts a **summary** list of accounts, and requires cable system operators to support their cost of service studies with a **report of their revenues, expenses, and investments** pursuant to **that** list of accounts. The Commission also decides to establish, after further steps described in the **Further Notice**, a uniform system of accounts for cable operators. **The uniform system** of accounts will apply only to operators that elect to set rates based on a cost of service showing. A **uniform** system of accounts will ensure that operators accurately and consistently record their **revenues, operating expenses, depreciation expenses, and investment**. In reaching this **decision, the Commission notes that accounting** records will serve as the principle source of information on cable operators that elect cost of **service** regulation and a uniform **system** will, therefore, help keep variations in accounting practices from unduly complicating cost of service proceedings.

Cost Allocation Requirements: The Commission adopts cost allocation rules that require cable operators to assign or allocate all costs and revenues identified in the summary level accounting form either to the equipment basket or to one of five service cost categories: basic service activities, cable programming service activities, other programming service activities, other cable activities, and noncable activities. To the extent possible, costs must be directly assigned to the category for which the cost is incurred. Where direct assignment is not possible, cable operators shall use allocation standards incorporated in current Section 76.924(e)(f) of the Commission's rules.

Affiliated Transactions: To keep cable system operators from engaging in improper cross-subsidization, the Commission adopts rules governing transactions between cable operators and their affiliates.

Procedural Requirements

Threshold Requirements for a Cost of Service Showing: There are no threshold requirements limiting the cable systems eligible for a cost of service showing, except for the two-year filing interval described below.

Historic Test Year: Cost of service showings shall be based on a historic test year, adjusted for known and measurable changes that will occur during the period when the proposed rates will be in effect. The test year should be the last normal accounting period. In the case of new systems for which no historic data is available, a projected test year may be used; the assumptions on which the projected test year are based will be subject to careful scrutiny.

Cost of Service Filing Interval: After rates are set under a cost of service approach, cable operators may not file a new cost of service showing to justify new rates for two years absent a showing of special circumstances.

Cost of Service Form: Commission adopts a form to be used by cable operators making cost of service showings. The Commission states that this form will be made available electronically as soon as possible.

Hardship Showing: In individual cases, the Commission will consider the need for special rate relief for a cable operator that demonstrates that the rates set by a cost of service proceeding would constitute confiscation of investment and that some higher rate would not represent exploitation of customers. The operator would be required to show that unless it could charge a higher rate it would be unable to maintain the credit necessary to operate and would be unable to attract investment.

The operator would also be required to show that its proposed rates are reasonable by comparing them to the rates charged by similar systems. In considering whether to grant such a request, the commission will consider the overall financial condition of the cable operator and other factors, such as whether there is a realistic threat of termination of service.

Small Systems

The Commission adopts an abbreviated cost of service form for use by small systems, to reduce the administrative burdens of cost showings for small system operators. The information must be certified by the operator as correct subject to audit by the Commission. The Commission solicits comments on the possibility of exempting small systems from uniform system of accounts requirements.

Streamlined Cost Showing for Upgrades

The Commission adopts a streamlined cost showing for upgrades. Under this showing, operators would be permitted to adjust capped rates by the amount of the net change in costs on account of the upgrade. Operators must reflect in rates any savings associated with upgrades and must apply cost allocation rules applicable to cost showings generally.

The Incentive Upgrade Plan

The Commission announces an experimental incentive plan that provides subscribers with assurances that rates for current regulated services will not be increased to pay for upgrades that are not needed to provide their current services and provides cable operators with incentives to upgrade their systems and offer new services. Specifically, operators will be given substantial rate flexibility for some established period of time in setting rates for new services. Operators that elect to operate under this plan will commit to maintaining rates for their current regulated services, including the basic service tier, at their current level. Operators also will commit to maintaining at least the same level and quality of service, including the program quality of their current regulated services.

Operators must seek Commission approval before setting rates for new services pursuant to the plan. New service tier8 comprised of new programming as well as new functions that can be used with existing tiers are eligible for this plan as long as they are available and chargeable on an unbundled basis from existing services.

The plan seeks to give cable operators a strong incentive to invest in their networks and increase the services they offer to

customers. This incentive is generated by giving the operator broad flexibility in setting the rates for these added services and capabilities. If the operator invests wisely **and** introduces **services** that meet customer needs, it gains the opportunity to achieve higher profits. The plan is intended to help achieve the **Cable Act's goals** of setting **rates similar** to those in competitive markets. As in competitive markets, customers are protected from monopoly rates for established services, but entrepreneurs who successfully introduce new products or improve the efficiency of their operations are rewarded through higher profits.

The Commission will entertain requests from operators seeking to use the plan on an experimental basis, and seeks comment on whether the plan should be **made permanent**. The Commission will accept proposals from operators as of the effective date of its cost rules.

Further Notice of **Proposed Rulemaking**

Pending completion of cable system cost studies **and** the development of experience through the **case-by-case** evaluation of complaints, the Commission is adopting the current rules on an interim basis. The Commission seeks comment on whether the rules should be adopted as permanent.

Among other issues, the Commission seeks **comment** on whether **11.25%** is an appropriate **rate of return** and on whether it should adopt an **average** cost schedule approach for **small systems**, and possibly for **larger systems** as well. The **Commission** delegates authority to the Cable **Services Bureau** to obtain detailed cost information **from cable operators** to help **examine this approach**. The Commission also seeks further data, analysis, and comment on whether to include a productivity factor in addition to an inflation factor in the benchmark/price cap formula. Based on the **current** record, the **Commission** proposes a **2%** productivity factor.

The uniform **system of accounts** proposed by the Commission in the **Further Notice** is derived in part from the **system** currently used by the **Commission** for telephone companies (see Part 32 of the **Commission's rules**), but the **Commission** seeks to simplify those **rules** and adapt them to the cable industry. The **Commission** requests that industry groups work with Commission staff to develop a **proposed uniform system** of accounts, with a view towards completion of a tentative proposal within 180 days. The Commission will then solicit comments from interested parties on the proposed uniform system of accounts before adopting a final version.



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February 22, 1994

EXECUTIVE SUMMARY

February 22, 1994

Implementation of Sections of the Cable Television Consumer
Protection and Competition Act of 1992;
Report and Order and Further Notice of Proposed Rulemaking
MM Docket No. 93-266

The Commission today adopted a Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking in MM Docket 92-266, Implementation of the Rate Regulation Provisions of the Cable Act of 1992. The Second Order on Reconsideration modifies, among other things, the Commission's previous benchmark approach for determining initial rates of regulated cable systems. The Commission's revised rules will better ensure that consumers are offered regulated services at reasonable rates, and will provide incentives for cable operators to launch new program services and invest in advanced technology. The modified rate regulations will apply to regulated rates in effect **on and after the effective date** of the new rules; regulated rates in effect before that date will continue to be governed by the old benchmark system.

The Revised Competitive Differential

The Commission's revised competitive differential is based on a strengthening of its statistical and economic **model** for estimating the difference between **rates** charged by noncompetitive systems and **systems** subject to "effective competition," as that term is defined in the **1992 Cable Act**. **The Commission's** model is based on a **survey of industry rates conducted by** Commission staff in the winter of 1992. **The competitive differential represents the Commission's best determination of the average amount by which the rates charged by a cable operator not subject to effective competition exceed "reasonable" rates.**

In response to comments made by petitioners on reconsideration, **and upon** further analysis by the staff, the Commission significantly improved its statistical analysis of the 1992 survey results. This effort has resulted in **a revised**

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benchmark formula that is both more accurate and more sophisticated. The revised benchmark formula will be used to help estimate the competitive differential and to determine which noncompetitive systems are covered by the phased implementation program described above.

In addition, the Commission revised its economic analysis to better evaluate the record evidence concerning the rates charged by the three types of systems Congress deemed subject to effective competition (i.e., systems with penetration rates of less than 30 percent, systems that face actual competition, and systems operated by municipalities). In the Rate Order adopted in this docket last April, the Commission computed the competitive differential by simply averaging the data for all of the systems that meet this statutory definition. On reconsideration, the Commission determined that the 1992 Cable Act required it to "take into account" the rates charged by the three different types of effectively competitive systems in determining-reasonable rates, but did not require it to use the methodology adopted last spring. In addition, the Commission determined that its previous methodology understated the competitive differential by weighing systems on the basis of the number of systems, rather than by evaluating which type of system best illustrates a competitive price.

Under the revised approach for determining the competitive differential, the Commission computed, and considered, the competitive differential for **each** of the three types of systems deemed *subject* to effective competition. After **analyzing** the various characteristics of the three types of effectively competitive systems, and exercising its expertise and discretion, the **Commission** determined that the best estimate of the **average** competitive differential is 17 percent.

The Commission will issue forms upon release of the Order for use in **applying the revised competitive differential to rates of regulated cable systems**. It also will help operators apply the revised benchmark formula by making Cable Service Bureau staff available to answer questions and by distribution of a **computerized spread sheet**.

Further Competitive Rate Rollbacks

Under the **Commission's** revised benchmark regulations, noncompetitive cable systems that have become subject to regulation will be required to set their rates at **a level equal** to their September 30, 1992 rates minus a revised competitive

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differential of 17 percent. Cable operators who seek to charge rates higher than those produced by applying the competitive differential may elect to invoke cost of service procedures the Commission also adopts today in a separate action:

Although all noncompetitive systems will potentially be subject to the new competitive differential, the Commission has adopted a phased implementation program which will give it more time to evaluate whether certain noncompetitive systems have lower than average competitive differentials. These systems include noncompetitive systems with relatively low prices (defined as systems whose rates would be below the benchmark after subtracting the 17 percent competitive differential from their September 30, 1992 rates or reducing their rates to the new benchmark level). The phased implementation program will also apply to systems owned by small operators (defined for this purpose as operators serving a total subscriber base of 15,000 or fewer subscribers and that are not owned or controlled by larger companies).

While the Commission collects additional cost and price data about the low priced and small operator systems, such systems will not be required to reduce their regulated rates immediately by the full competitive differential. Rather, implementation of the full differential will be stayed pending completion of the Commission's cost inquiry. At the same time, to protect consumers while the cost studies are being conducted, a system subject to phased implementation will be required to calculate the extent to which its rate reduction falls short of 17 percent. This reduction "deficit" will then be offset against any inflation adjustment pending completion of the cost studies.

The Price Cap Governing Cable Service Rates

Calculation of External Costs In addition to revising the benchmark formula and the competitive differential used in setting initial regulated cable rates, the Commission adopted rules to simplify the calculations used to adjust those rates for inflation and external costs in the future. Under current rules, operators may adjust their regulated rates annually by inflation and up to quarterly by the net change in external costs. Any change in external costs must also be measured against inflation and adjusted for the corrected inflation rate. To simplify these rate-adjustments, the Commission has separated the inflation adjustment from the external cost adjustment. This refinement will reduce the administrative burden associated with seeking a rate increase. A form to be released with the Order will set forth the specific steps for making these calculations.

Copyright and Pole Attachment Fees. The Commission also determined to treat increases in compulsory copyright fees incurred by carrying distant broadcast signals as external costs in a fashion parallel to increases in the contractual costs for nonbroadcast programming. The Commission will not, however, accord external cost treatment to pole attachment fees.

"A La Carte" Packages

The Commission also revised its regulatory treatment of packages of "a la carte" channels. In its April 1993 Rate Order, the Commission exempted from rate regulation the price of packages of "a la carte" channels if certain conditions were met. On reconsideration, however, the Commission determined that its rules governing the provision of "a la carte" channels in a package should be refined to better ensure that the marketing of channels in this fashion is designed to enhance subscriber choice rather than evade rate regulation. When assessing the appropriate regulatory treatment of "a la carte" packages, the Commission will consider certain factors, among other considerations, that would suggest that packages should not qualify for non-regulated treatment, including : whether the introduction of the package avoids a rate reduction that otherwise would have been required under the Commission's rules; whether an entire regulated tier has been eliminated and turned into an "a la carte" package; whether a significant number or percentage of the "a la carte" channels were removed from a regulated service tier; whether the package price is deeply discounted when compared to the price of an individual channel; and whether the subscriber must pay significant equipment or other charges to purchase an individual channel in the package. In addition, the Commission will consider factors that will reflect in favor of non regulated treatment such as whether the channels in the package have traditionally been offered on an "a la carte" basis or whether the subscriber is able to select the channels that comprise the "a la carte" package. "A la carte" packages which are found to evade rate regulation rather than enhance subscriber choice will be treated as regulated tiers, and operators engaging in such practices may be subject to forfeitures or other sanctions. This process will be conducted on a case-by-case basis.

Small Systems

The Commission also lifted the stay of rate regulation for small cable systems, which were defined as all systems serving 1,000 or fewer subscribers. Thus, as of the effective date of the Commission's new rules, noncompetitive, small systems will be

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subject to rate regulation. (The Commission will entertain requests for extensions of time to comply if operators of small systems meet certain showings requirements). To reduce the regulatory burdens, particularly the equipment cost calculations, that rate regulation imposes on small systems, the Commission also adopts two types of administrative relief for small systems.

First, the Commission suspended, pending development of average equipment cost schedules, the requirement for unbundling equipment and installation charges, and permitted a simple across-the-board reduction in each individual regulated rate separately billed by the operator. This relief **allows operators** of such systems to reduce their overall rates and the **rate** for each regulated component (programming or service) by the revised competitive differential, without the need to complete a Form 393 or to prepare a cost-of-service showing. This administrative relief is available to independently owned small systems and small systems owned by small operators. The Commission defined a small operator for purposes of obtaining administrative relief as an operator that has 250,000 or fewer total subscribers, owns only systems with fewer than 10,000 subscribers each, and has an average system size of 1,000 or fewer subscribers.

Second, the Commission decided **to permit larger operators** of small **systems** to use **the average equipment costs of its small systems in setting rates in individual franchise areas.** The Commission defined a larger operator of small systems as one that **owns more than one cable system, one of which has 1,000 or fewer subscribers, and is not a small operator as defined above.**

The Commission **also determined that it would later provide additional administrative relief for small systems by developing an average equipment cost schedule that can be used by all small systems to unbundle their equipment and installation revenues and rates. The cost schedule will be based on industry-wide figures derived from the Commission's cost survey (to be conducted over the next-? twelve to eighteen months.)** Such a schedule will ultimately be made available for use by all operators as part of the Commission's efforts to simplify its procedures.

Adjustments to Capped Rates for Addition and Deletion of Channels

In the Fourth Report and Order the Commission also adopted a methodology for determining rates when channels are added to or deleted from regulated tiers. This methodology **is similar to the third alternative proposed in the Third Further NPRM.**

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In order to determine **rates** following the addition or deletion of channels, each operator, after applying the revised competitive differential, will adjust its per channel rates to reflect the proportionate decrease in per channel rates captured by the Commission's rate survey, based on the total number of regulated channels. Under this approach, cable system operators must pass on to subscribers the efficiencies and economies of scale that arise **as** operators add channels to their systems.

The Commission also will treat programming costs as external costs, to be calculated under the methodology described in the Rate Order as modified by our Reconsideration Orders. Thus, operators **may** recover the full amount of **programming expenses** associated with added channels. This will help **promote** the growth and diversity of **cable programming** to the benefit of subscribers, cable operators, and programmers. Operators may also recover **a** mark-up **on** their programming expenses.

The Commission **stated that** its methodology will provide a ready way for operators to determine **rates** when **new programming services** are added to regulated offerings and will not be **unduly burdensome** for **subscribers, operators, and regulators**. It is also fully consistent with the **revised approach to setting** initial regulated rates, **can be used for deletions of channels** and moving **channels among** regulated tiers as well as **for channel** additions, and protects **subscribers on one tier from having their rates raised by changes on other tiers**. Cable operators will use an FCC Form, to be released with the text of the Commission decision, to **adjust capped rates when channels are added to or deleted from regulated tiers, and to make external cost and inflation adjustments**.

Adjusting Capped Rates for Cable Systems Carrying More Than 100 Channels

Finally, in the Fifth Notice of Proposed Rulemaking, the Commission seeks **comment** on whether it **should** establish a benchmark methodology for adjusting capped rates when a cable system carries more than 100 regulated channels, and if so, what that methodology should be.



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Executive Summary

THIRD ORDER ON RECONSIDERATION IN CABLE RATE REGULATION AND TIER BUY-THROUGH PROCEEDINGS (MM DOCKET NOS. 92-266 AND 92-262)

Today the Commission adopted a Third Order on Reconsideration in MM Docket Nos. 92-266 (Rate Regulation) and 92-262 (Tier Buy-Through Provisions). Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992.

This notice summarizes the actions taken in the Third Order on Reconsideration.

1. The 1992 Cable Act provides for regulation of cable services where a cable system does not face "effective competition," and the Act provides three specific tests for determining which systems face effective competition. The second test finds effective competition where there is at least one alternative multichannel service provider that reaches at least 50% of the households in the franchise area, and at least 15% of the households in the franchise area subscribe to such alternative service(s).

The item adopted today affirms the Commission's rules for determining the presence of effective competition, as adopted on April 1, 1993, in the following ways:

- * the subscribership of competing multichannel distributors will be considered on a cumulative basis to determine if it exceeds 15%, but only the subscribers to multichannel providers that offer programming to at least 50% of the households in the franchise area will be included in this cumulative measurement;
- * Satellite Master Antenna Television Systems (SMATV) and Satellite Television Receive Only (TVRO) subscribership in an area may both be counted, generally, toward meeting the 15% test, since satellite service is generally available from at least one of these complementary sources; and

2. This Order clarifies that, for purposes of all three parts of the 1992 Cable Act's definition of **effective competition**, housing units that are used solely for seasonal, occasional or recreational use **should not** be counted. Therefore, a system will **not** be exempted from rate regulation as a "low penetration" system if the reason for the low penetration rate is that a large number of the **households** are unoccupied.

3. With regard to the 1992 Cable Act's requirement that cable operators have a rate structure that is uniform throughout the cable system's geographic area, the Order reaches the following decisions:

- * cable operators may offer nonpredatory bulk discounts to multiple dwelling units (MDUs) if those discounts are offered on a uniform basis to buildings of the same size with contracts of **similar** duration. Rates cannot be **negotiated individually** with MDUs;

- * cable operators' existing contracts with MDUs are **grandfathered** to the extent they are in compliance with rate regulation; and

- * the uniform rate structure requirement applies to all franchise areas, regardless of whether the cable system is exempt from **rate regulation** because of the presence of **effective competition**. Therefore, a cable operator **charging** competitive rates where it is subject to effective competition is **prohibited from charging** higher **rates** elsewhere.

4. The tier buy&rough provision of the 1992 Cable Act prohibits cable operators from requiring subscribers to **purchase** anything **other** than the **basic** service **tier in order** to obtain access to **programming offered** on a **per-channel or per-program** basis. The Order affirms that this provision **applies** to all cable systems, **including those that are** not subject to rate regulation.

5. This order **takes the** following actions with regard **to the process** of **certifying** local franchising authorities to regulate cable service:

- * it affirms the Commission's decision that, at this time and in most circumstances, it will not assert jurisdiction over basic cable service where franchising authorities have chosen not to regulate rates;

- * it affirms the Commission's determination that franchising authorities seeking to have the Commission regulate basic rates must demonstrate that proceeds from their franchise fees will not cover the costs of rate regulation;

- * it allows franchising authorities to voluntarily withdraw their certifications if they determine that rate regulation is no longer in the best interest of local cable subscribers and they have received no consideration in exchange for their decision to decertify;

- *** affirms** the Commission's jurisdiction **over** basic rates **when** a **franchising authority's certification** is denied for lack of legal authority or for failure to adopt regulations **consistent** with the Commission's **rate** rules; and

- * **ic** allows a franchising authority to cure any nonconformance with the Commission's **rules** that does not involve a substantial or material regulatory conflict before the Commission **revokes** its **cenificacion** and assumes jurisdiction.

6. The Order takes **the** following actions with regard to franchising authorities basic rate regulation:

- * establishes procedures whereby **the** Commission will make cost determinations for **the** basic service tier, when requested by local franchising **authorities**, **in an** effort to assist franchising **authorities** whose limited **resources** may preclude **conducting** cost-of-service **proceedings**;

- * **affirms** franchising authorities' right to order cable companies to provide refunds upon a determination that basic tier **rates** are **unreasonable**;

- * **clarifies** that **franchising** authorities may **delegate their rate** regulation responsibilities to a **local commission** or other subordinate entity, if so authorized by **state and/or** local law;

- * **affirms** **the** Commission's **decision** that cable **operators** may not enter into **settlement agreements** with franchising authorities **outside the scope of the** Commission's **rate regulations**, but **states that the** parties may **stipulate** to any **facts** for which there is a basis in the record;

- * **clarifies** that franchising authorities are entitled to request information from the cable operator, including proprietary information, that is reasonably necessary to support assertions made by the cable operator on Form 393 as well as those made in a cost-of-service showing, but **modifies the** Commission's position on the confidentiality of such proprietary information by determining that state and local laws will govern such issues;

- * **clarifies that, to the extent** that franchise fees are calculated as a percentage of gross revenues, franchising authorities must **promptly return overpayments of franchise** fees to cable operators that result from the cable operator's newly-diminished gross revenues after refunds (or allow cable operators to deduct such overpayments from **future payments**);

- **reminds franchising authorities** that **they may** impose **forfeitures and fines** for violations of **their rules, orders, or decisions**, including the **failure to file** requested information, if permitted **under state or local law**; and

. modifies the Commission's rules to require that cable operators comply with franchising authorities' requests for information, as well as those made by the Commission.

7. The Order takes the following actions with regard to Form 393 (filed by cable operators with their local franchising authority once that authority has certified to regulate cable service, and with the Commission in response to a subscriber complaint):

*** informs franchising authorities that, if a cable operator fails to file a Form 393, they may deem the operator in default. find that the operator's rates are unreasonable, and order appropriate relief, such as a refund and a prospective rate reduction:**

*** informs franchising authorities that they may order a cable operator to file supplemental information if the cable operator's form is facially incomplete or lacks supporting information, and the franchising authority's deadline to rule on the reasonableness of the rates will be suspended pending the receipt of the additional information;**

*** prohibits filings on anything but an official FCC Form 393 or a photocopy, orders cable operators that have filed on a non-FCC form with the Commission to refile on an official form within 14 days after the effective date of this Order, and entitles the franchising authority to similarly order a refiling by a cable operator that has filed on a non-FCC form within 14 days from the effective date of this Order; and**

*** reminds franchising authorities that they have the discretion to resolve questions or ambiguities regarding the application of the rate-setting process to individual circumstances and that, if challenged on appeal, the Commission will defer to the franchising authority's decision if supported by a reasonable basis.**

8. The Order continues to require that, when advertising rates, cable operators disclose costs and fees, but cable operators advertising for multiple systems on a regional basis may advertise a range of actual total prices, without delineating the specific fees for each area.

9. Identifies certain cable operator practices as possible evasions or violations of the Commission's rate regulations and tier buy-through prohibition, such as:

*** moving groups of programming offered in tiered packages to a la carte;**

*** collapsing multiple tiers of service into the basic tier;**

*** charging for services previously provided without extra charge**

* **charging** for services previously provided **without** extra charge (e.g. **routine** services, program guides) **unless** the value of **that** service, as now **reflected** in the new charges. was taken **out** of **their** basic rate number when calculating the reduction necessary to establish reasonable rates.

* assessing downgrade charges for service packages that were added without a subscriber's **explicit** consent.

10. The order recognizes that **the** 1992 Cable Act provides that the Commission and **the states** have concurrent jurisdiction to regulate cable operators' negative option billing practices and that **the 1992** Cable Act does not **preempt** the states from regulating those practices under state consumer protection laws.

11. The Order makes the following determinations with regard to equipment and installation:

* the rate-setting process already reflects **promotional costs and seasonal maintenance costs**; therefore, rates **may not** be raised **to reflect such costs**; and

* **no special schedule** for **calculation** of **charges for home wiring** is **needed** when that wiring is offered for sale to **subscribers upon termination of cable service**.

Action by the **Commission February 22, 1994**, by Third **Order on Reconsideration** (FCC 94-___). **Chairman Hundt, [etc.]**

-FCC-

News **Media Contact: Karen Watson** or Susan **Sallet** at **(202) 632-5050**
Cable **Services Bureau contacts: Amy J. Zoslov** at **(202) 416-0808** and **Julia Buchanan** at **(202) 416-1170**.



NEWS

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Report No. DC-

ACTION IN DOCKET CASE

February 22, 1994

FCC ORDERS FURTHER **RATE** REDUCTIONS WHILE PRESERVING INCENTIVES FOR CABLE OPERATORS TO INVEST IN **NEW** SERVICES

The Commission today completed the first round of rate regulation to implement the Cable Television Consumer Protection, and Competition Act of 1992. The Commission unanimously adopted a comprehensive package including revised rate regulation rules; rules and procedures allowing cable operators to present a cost-of-service showing; and an item involving reconsideration of other regulation items adopted last April.

"These regulations are fair to cable subscribers, who will pay reasonable rates, and fair to cable operators, who have strong incentives for investment and innovation," Chairman Reed Hundt said today. "We aren't claiming our job is over, but rather that our first step is completed. These regulations will result in consumers paying less for the same services or receiving more for the same money," Chairman Hundt added.

Upon reconsideration of its original benchmark regulation, the Commission decided to require that prices for regulated services of all cable systems be lowered 17 percent. This reduction will be reached through a two-step process.

The Commission took the first step on April 1, 1993, when it required systems operating above a price benchmark average to come down 10 percent. That action caused the prices of about two-thirds of all systems to drop when comparing the same package of regulated services. The Commission takes the second step, to bring prices down another 7 percent, today. This will cause about 90 percent of cable systems to drop prices for the same package of regulated services.

The Commission also adopted going forward rules designed to preserve the incentives for the cable industry to continue building the National Information Infrastructure and to add creative new programming services to its cable offerings. Cable operators will be able to add value to their regulated packages of cable services and to create new, unregulated services.

(over)

The FCC's implementation of the 1992 Cable Act has already brought an end to the rapid price increases in cable services that occurred following the implementation of the 1984 Cable Act. In addition, the Commission has adopted rules that go a long way toward improving customer service. Had the 1992 Cable Act not been passed, prices would have continued to rise and consumers would have paid more for the same services than they will in 1994.

Cable operators below the new benchmark and small cable operators will have a transition period during which they will not be required to lower their prices by the full 17 percent pending the completion of cost studies. In addition, certain small systems will also be relieved of the requirement to unbundle equipment revenues and rates, a requirement which appears to have placed a large burden on small operators.

The Commission adopted rules and procedures for **cost** of service rate showings. Under these regulations, a cable operator may request relief from the required reduction in rates by showing that its costs of service are unusually high. The cable cost of service policies adopted today are similar to those the Commission has applied to the telephone industry. This traditional cost of service approach balances the interests of the cable operators and their customers, permitting operators to recover from customers only the reasonable costs of providing regulated services, including operating expenses and a reasonable rate of return. Included in our cost-of-service rules is a provision for streamlined showings by small operators, yet another mechanism for lightening the regulatory burden on small systems.

The final item adopted by the Commission today affirms earlier decisions by the Commission, such as the tier buy-through provisions. Under this provision cable **operators cannot** require a subscriber to purchase any level of **service** other than the basic service in order to **access** pay-per-view and other premium channel offerings.

The Commission is undertaking **an** aggressive effort of education and assistance in order to maximize the effective implementation of these regulations. In December, the Commission created a stand-alone Cable Services Bureau to provide "**one** stop shopping" for cable operators, consumers and state and local government officials, including franchising authorities.

Telephone assistance in obtaining and completing forms as well as other aspects of compliance with and implementation of these new regulations is available through the Bureau. A separate contact list, released today, is based on geographic zones and directs people to the correct Cable Services Bureau staffers. The Commission is also holding regional educational seminars for franchising authorities, other government officials and consumer representatives and a teleconference seminar for cable operators.

In adopting these items, the Commission also noted that implementation of the 1992 Cable Act depends on the participation of state and local franchising authorities, who must seek certification to regulate basic cable service, and consumers, who must complain to the Commission where they feel the Commission's regulations are being violated with respect to cable programming services. The Commission also looks forward to the full participation of the cable industry in implementing regulations that have the potential to bring value to the country as a whole.

Action by the Commission February 22, 1994, by

-FCC-

News Media contact: Karen Watson or Susan Sallet at (202) 632-5050

Cable Services Bureau contact: Sandy Wilson at (202) 416-0856

CABLE PROGRAMMING SERVICE RATE COMPLAINT FORM INSTRUCTIONS

The Federal Communications Commission (FCC) investigates the reasonableness of rates for cable programming service based on complaints filed by subscribers and local and state governments. By filing this form, you begin an investigation of your cable system's rates for cable programming service. Therefore, your participation is critical to the enforcement of the FCC's cable rate regulations.

Please read the following information before completing the attached Cable Programming Service Rate Complaint Form.

Who Regulates Cable Rates?

When you subscribe to cable television, your cable system offers you the option of choosing from among different programming packages. Some packages are regulated by the FCC and others by your local franchising authority.

The Federal Communications Commission is the federal administrative agency charged with regulating communications by radio, television, wire, satellite and cable.

A franchising authority is the local municipal, county or other government organization that regulates your cable television service at the state or local level. The name of your local franchising authority should be on the front or back of your current cable bill. If the information is not on your bill, contact your cable company or your local government.

What Do Local Franchising Authorities Regulate?

In most instances, your local franchising authority is responsible for regulating

- o Rates for basic cable service, equipment used to receive basic cable service, and installation and service charges related to basic service. The term "basic service" refers to the lowest level of cable service you can buy, and is the program package that includes signals from local television stations (such as ABC, NBC and CBS affiliates and Independent television stations) and public, educational and governmental access channels. Your cable system may use other terms to describe this service.
- o Customer service -- for instance, complaints about bills, a cable system's response to inquiries about signal quality and a cable system's response to service requests.
- o Franchise fees -- the fees paid by the cable system to the franchising authority for the right to offer cable service.

You should contact your local franchising authority if you believe your rates for basic service, related equipment or installation are unreasonable. Your local franchising authority will tell you if it is not responsible for regulating these rates.

You should contact your local franchising authority, and not the FCC, with complaints regarding customer service and franchise fees.

What Cable Rates Does the FCC Regulate?

The FCC regulates the rates you pay for certain programming that the FCC refers to as cable programming service. "Cable programming service" includes all program channels on your cable system that are not included in basic service and are not separately offered as pay-per-channel programming or pay-per-program services.

The FCC also regulates rates for equipment used solely to receive cable programming service and installation and service charges related solely to cable programming service. However, since most equipment used to receive cable programming service is also used to receive basic service, equipment complaints should generally be directed to your local franchising authority.

Are There Some Rates That Neither the FCC Nor Local Franchising Authorities Regulate?

Yes. Neither the FCC nor your local franchising authority regulates rates for pay-per-channel programming (for instance, a premium movie channel such as HBO or Showtime) and pay-per-program services (for instance, pay-per-view sports events). Therefore, you should not file a complaint about these services with the FCC or your local franchising authority.

Who Should Fill Out This Form?

You should fill out this form and submit it to the FCC if you are a cable subscriber wishing to file a complaint with the FCC about rates for cable programming service, related equipment or installation. Franchising authorities and other relevant state or local governments may also use this form to file a complaint with the FCC about rates for cable programming service, related equipment or installation.

How Does the Complaint Process Work?

Your complaint begins a legal process that requires your cable company to demonstrate that its rates are reasonable under the law.

The FCC requires your cable company to respond in writing to your complaint within thirty days of the date you file your complaint, unless your cable company is notified by the FCC that your complaint cannot be processed. In its response, your cable company must show that its rates are reasonable under the law. The cable company must provide you with a copy of its response. The FCC will examine the information submitted by the cable company and determine whether its rates for cable programming service are too high. If so, the FCC may order a refund and/or a rate reduction for the cable programming service. You and the franchising authority will receive a copy of the FCC's final ruling on the reasonableness of the cable programming service rate charged by your cable company.

Your complaint will be maintained by the FCC under the cable company's community unit identifier, which is a number assigned to each cable system by the FCC for administrative purposes. This number should appear on your cable bill. Your complaint will not be filed under your name. If you have a question concerning the status of your complaint, you may call (202) 416-0919. Please be prepared to tell us the name of the cable system and the name of the community where the cable system is located.

How To Fill Out This Form

1. You should use this form only to complain about rates for cable programming service, related equipment or installation, as described above.
2. In order to complete this form, you will need a copy of your current cable bill and the name and address of your local franchising authority. The name and address of your local franchising authority should appear on the front or back of your cable bill. If it does not, you must contact your cable company or your local government to obtain this information. We cannot process your complaint unless you include this information!
3. You may ask your local franchising authority for assistance in filling out this form. You may also attach a statement from your local franchising authority describing its views about the cable programming service rate in question. However, this is not a requirement.
4. Please fill in all information requested on this form. If you do not do so, we may not be able to process your complaint.
5. By submitting this form, you are stating your belief that your cable company's rates for your cable programming service, related equipment or installation are unreasonable.
6. If you have any questions about how to fill out this form, you may call the FCC at (202) 4160902.

FCC NOTICE TO INDIVIDUALS REQUIRED BY THE PRIVACY ACT AND **THE** PAPERWORK REDUCTION ACT

The solicitation of personal information in this form is authorized by the Communications Act of 1934, as amended. The Commission will use the information provided in this form to determine the reasonableness of a cable company's rates. In reaching that determination or for law enforcement purposes, it may become necessary to provide personal information contained in this form to another government agency. All information provided in this form will be available for public inspection. Your response is required to initiate and pursue your complaint.

Public reporting burden for this collection of information is estimated to average 45 minutes including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing the burden, to the Federal Communications Commission, Records Management Division, AMD-PIRS, Washington, D.C. 20564, and to the Office of Management and Budget, Paperwork Reduction Project (3060-0549), Washington, D.C. 20503. Do **not** send completed forms to these addresses.

THE FOREGOING NOTICE IS REQUIRED BY THE PRIVACY ACT OF 1974, P L. 93-579, DECEMBER 31, 1975, 5 U.S.C. 522(A)(e)(3) AND THE PAPERWORK REDUCTION ACT OF 1980, P L. 96-511, DECEMBER 11, 1980, 44 U.S.C. 3507